

UNITED STATES ENVIRONMENTAL PROTECTION AGENCY

WSG 7

Date Signed: December 13, 1976

MEMORANDUM

SUBJECT: Guidance on Allowable Costs for State Public  
Water System Supervision Program Grants

FROM: Alan Levin, Director (signed by Alan Levin)  
State Programs Division  
Office of Water Supply (WH-550)

TO: Regional Water Supply Representatives

This guidance has been prepared in partial fulfillment of Headquarters Commitment No. 15 listed in my memorandum of September 29, 1976. It is intended to familiarize you with those costs that are incurred by the States for public water system supervision programs that can be considered allowable for Federal grant participation within the Statutory and Administrative limitations.

**\*Note: CFR references may need to be updated due to upcoming revisions with the CFR.**

Guidance on Allowable Costs for State  
Public Water System Supervision Program Grants

1. Purpose

A number of States are incurring expenditures not only on the activities that are necessary for the implementation of the provisions of the Safe Drinking Water Act but also on water supply related activities that are mandated by their own State laws. Obviously, the Federal government cannot pay for activities that are required by the State laws in excess of federal requirements. For Federal grant participation, only those State costs are allowable which are related to the program elements authorized by Section 1413 of P.L. 93-523 and 40 CFR Section 35.626-1. This Guidance is expected to provide general information about the allowable costs as they relate to the State Public Water System Supervision Program.

2. Background

Section 1443 of P.L. 93-523 authorizes the Administrator to make grants to qualified States to carry out public water system supervision programs. Such grants shall cover not more than 75 per cent of the grant recipients' costs (as determined under regulations of the Administrator) that are necessary and reasonable to carry out program responsibilities. These costs are termed as allowable costs.

3. Allowable Costs

EPA Regulation 40 CFR Section 30.705 describes the following general criteria for determining the allowability for project (public water system supervision program in the present case) costs:

- (a) The cost must be reasonable and within the scope of the project;
- (b) The cost is allocable to the extent of benefit properly attributable to the project;
- (c) Such costs must be accorded consistent treatment through application of generally accepted accounting principles;
- (d) The cost must not be allocable to or included as a cost of any other federally assisted program in any accounting period (either current or prior); and
- (e) The cost must be in conformity with any limitations, conditions, or exclusions set forth in the grant agreement or this subchapter (B of 40 CFR), including appropriate Federal cost principles of this subpart (F of 40 CFR).

Expenditures for public water system supervision can be reported either by object class categories or by program elements.

### 3.1 Determination of Allowable Costs When Expenditures are Reported by Object Class Categories

When the expenses for the public water system supervision program are reported by object class categories such as expenditures for personnel administration, employee fringe benefits, travel, budgeting, payroll preparation, materials and supplies, etc., the allowability or non-allowability of reported expenditures can be determined by applying the principles outlined in FMC 74-4 of July 18, 1974 "Cost Principles Applicable to Grants and Contracts with State and Local Government." This document contains excellent background information and guidance for the proper treatment of cost in 27 object class categories. Additional guidance may be found in the Grant Administration Manual under the following parts:

- a. Part 6 - Price/Cost analysis and Cost Review
- b. Part 7 - Determination of Cost (this part also includes a copy of FMC 74-4)
- c. Part 8 - Cost Sharing

### 3.2 Determination of Allowable Cost When Expenditures are Reported by Program Elements

When the expenses for the public water system supervision program are reported by program elements, they must be for program elements authorized by Section 1413 of the Act and 40 CFR Section 35.626-1. Expenditures incurred in carrying out the program elements listed in 40 CFR Section 35.626-1 (or any other appropriate program elements) are allowable costs provided that the expenditures:

- (a) Are incurred specifically for the public water system supervision program;
- (b) Benefit both the public water system supervision program and other related work and can be distributed to them in reasonable proportion to the benefits received or;
- (c) Are necessary to the overall operation of the grantee, although a direct relationship to any particular cost objective cannot be shown.

### 3.2.1 Unallowable Program Element Costs

Certain costs incurred on the program elements listed in 40 CFR Section 35.626-1 might appear to be allowable costs but they are not allowable because they are contrary to EPA policy. A list of such unallowable costs will evolve as more experience with the implementation of grant regulations is accumulated. At this time only the following two types of costs deserve mention:

- (a) The costs to collect routine monitoring samples should be the responsibility of public water systems. Therefore, State expenditures for collection of routine monitoring samples are unallowable costs for Federal grant participation. With respect to the acceptability of State expenditures to analyze routine monitoring samples as allowable costs, the preamble to the final regulations dated January 20, 1976 for State Public Water System Supervision Programs pointed out "that such costs should be transferred to the public water systems as quickly as feasible." However, in response to pertinent comments, no limitation on the use of grant funds to analyze routine monitoring samples was included in the grant regulations. Instead, a more practical and conciliatory approach was adopted in the sense that "if experience later indicates that a restriction is desirable, States which provide routine sample analysis for public water systems will be given ample time to phase out their programs or find additional funding."
- (b) In instances where the State provides personnel to design, construct and operate State-owned public water systems in addition to the Plan Review activity, the expenditures incurred on such additional activities are unallowable costs and should be borne entirely by the State.

### 3.2.2 Maintenance of Expenditure Records

Eventually, some of the grants awarded to the States will be audited. Therefore, it is imperative that the expenditures are reported properly to avert subsequent audit problems. In this context it is suggested that "Audit Guide for EPA Grants (other than construction Grants)" should also be used for additional information. This document provides, in Chapter 3, examples of unallowable, unreasonable, improperly allocated, improperly documented, and improperly approved costs.